



April 1, 2011

Ms. Susan M. Cosper
Technical Director
Financial Accounting Standards Board
401 Merritt 7, P.O. Box 5116
Norwalk, CT 06856-5116

File Reference No. 2011-150

Re: Supplementary Document: Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities – Impairments

Dear Ms. Cosper:

The Loan Syndications and Trading Association (LSTA)¹ appreciates the opportunity to comment on the Supplementary Document: *Accounting for Financial Instruments and Revisions to the Accounting for Derivative Instruments and Hedging Activities – Impairments* (the proposal).

The LSTA strongly supports the convergence efforts of the Financial Accounting Standards Board (FASB or the Board) and the International Accounting Standards Board (IASB), collectively the Boards. However, we find that it is difficult to provide a meaningful response to the proposal in a short period of time without the benefit of understanding the other critical components of an impairment model, including estimation of loss factors, non-accrual loans, troubled debt restructurings, purchased loans and debt securities with credit deterioration. We also have concerns that the IASB and FASB are at different stages in their deliberations, which may result in differences in the final standards issued by the Boards. Because the impairment guidance is a topic that has critical importance to the global capital markets, we believe that it is imperative that the Boards work together to coordinate timing of the requirements and urge that the

¹The LSTA represents over 300 of the largest US and foreign banks, broker dealers, hedge funds, mutual funds, insurance companies, and institutional investors. The LSTA was founded in 1995 with the objective to improve liquidity and transparency in the floating rate corporate loan market. As the principal advocate for this asset class, the LSTA fosters fair and consistent market practices to advance the interest of the marketplace as a whole while promoting the highest degree of confidence for investors of corporate loans. The LSTA undertakes a variety of activities to develop policies and market practices designed to advance just and equitable marketplace principles and to encourage coordination with firms, facilitating transactions in loans and related claims.



impairment guidance is closely coordinated with the FASB's efforts on the broader project dealing with Accounting for Financial Instruments.

We are equally concerned that the proposals would not be viable for smaller balance high volume loans, as it would be operationally difficult and time consuming to segregate portfolios (between the good book and the bad book) that are managed typically on a collective basis.

We are also concerned about consistency and comparability in the determination of the "foreseeable future" and segregation of loans into a good book and bad book. If regulators in certain jurisdictions prescribe the foreseeable future to be a specific time frame depending upon the type portfolio or prescribe the bases for which segregation should be applied, then this will result in lack of comparability and a lack of a level playing field if different jurisdictions apply different interpretations adversely impacting certain financial institutions compared to those in other jurisdictions. Additionally, members of the LSTA find the examples provided in paragraph B3 of the proposal unclear and would prefer to use the current definition of impairment in ASC 310.10.35-16 to determine that a loan should be placed in the bad book. This definition is well understood and not the cause of the today's concern with the current incurred loss impairment model.

While some of our member institutions have not had sufficient time to adequately and fully evaluate the proposed model and assess the implications it may have on their financial statements and related operational processes thereof, we believe the proposed model generally will expedite the recognition of a greater allowance relative to the current incurred loss models under US GAAP and IFRS. However, simply increasing the allowance should not be the objective without an overriding principle that we are seeking to achieve. Other equally important objectives include providing a model that is operational and cost-effective to apply, that produces a provision and an allowance for loan losses that provide meaningful information to investors and other key stakeholders.

As indicated above, the LSTA supports the Boards' efforts to propose a converged model, but we are concerned that the resulting proposal to use the higher of the (a) time-proportional amount (TPA) of losses for the remaining life; and (b) expected losses in the foreseeable future can only be described as a compromise of principles between the Boards rather than an internally consistent model that provides the best information for external reporting. We commend the Boards for trying to develop a single converged standard, but we cannot support such a standard if it requires preparers to implement two separate models that would require updating at each reporting date. We also believe that the converged model results in unnecessary complexity for both preparers to operationalize and investors/users of financial statements to understand. Specifically, we believe that the pattern of loss recognition under the TPA is both complex and has variable bases for measurement which will likely be difficult to explain to investors and analysts as it is not based on any conceptual basis and is not consistent with credit risk management techniques. For example, application of the principles at the portfolio level can result in some portfolios being booked based on the floor while others are recorded at the TPA. The aggregate amounts are difficult to understand and the measurement bases for each portfolio



can, and likely will, change over time due to changes in economic conditions and/or changes in underwriting behavior. We believe that these realities complicate and potentially obscure the core information that users seek from financial statements: how did key indicators of credit quality and loss experience change during the reporting period and how are those changes reflected in your allowance and provision for losses during the period.

In addition, the TPA appears operationally challenging to apply for some institutions as it will require systems enhancements to calculate the weighted average age and life of the portfolio at each reporting date. For every open pool of loans, a reporting entity will be required to make three measurements: (1) the amount of expected losses in the good book based on the time-proportionate amount, (2) the amount of expected losses in the good book based on the incurred loss/foreseeable future floor, and (3) the amount attributable to the bad book. Some institutions believe it will be difficult to isolate the TPA associated with specific loans upon transfer to the “bad book” and then recalculate the allowance for both bad and good books. With many loan products, we think the greater amount will be the floor (if the floor is greater than 12 months, as currently proposed) because the losses are expected to occur early in the life of the loan and as such there is no a benefit in calculating the TPA. One alternative would be to reserve the floor amount for the good book rather than performing the “higher of test”. Another alternative would be to set the floor based upon a longer loss emergence period than is currently applied today for the portfolio, rather than the foreseeable future. Further, we have concerns about comparability between institutions’ financial statements resulting from choices in discounting, discount rates, and of TPA methodology selected (i.e., straight line or annuity) as permitted under the proposal.

Concerning disclosure, we recognize that this has not yet been addressed but would recommend that there should be converged IASB and FASB guidance on disclosure around credit risk/credit quality. In this regard, we recommend that the IASB and FASB look to the IFRS 7 disclosures and US GAAP credit quality disclosure requirements and incorporate the most useful disclosures from each to create a uniform level of disclosure by all financial institutions reporting under IFRS and US GAAP.

To reiterate our position as discussed in the LSTA’s comment letter regarding the FASB’s proposed Accounting Standards Update, *Accounting for Financial Instruments and Revisions to the Accounting for Derivative and Hedging Activities*, the LSTA supports a framework in which a single impairment model for both originated and purchased credit impaired loans is applicable for all financial instruments not carried at fair value. A single impairment model will reduce the current complexity in accounting for financial instrument impairment and is consistent with the objective of developing principles based standards. Consistent with this view, the LSTA does not support the continuation of a different impairment model that is specifically applicable to purchased financial assets with credit deterioration. Rather, the LSTA supports an impairment model that allows an entity that purchases a financial asset to establish an allowance for credit losses upon acquisition that is determined through the normal credit review process and subsequently maintains that allowance on a basis consistent with the methodology for originated financial assets. Also, regarding the scope of the proposal, the narrow focus on open portfolios



makes it difficult to determine how the model will apply to individual loans and closed portfolios.

We truly appreciate the opportunity to share the loan industry's perspective on the proposal. If you have any questions concerning our comments or suggestions, please contact Sherif Sakr at (212) 436-6042, Melanie Pinto at (212) 276-1537 or Ellen Hefferan at (212) 880-3013.

Yours truly,

A handwritten signature in black ink, appearing to read "Sherif Sakr". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

Sherif Sakr
Co-Chair LSTA Accounting Committee

A handwritten signature in black ink, appearing to read "Ellen Hefferan". The signature is cursive and somewhat stylized, with a long horizontal stroke at the end.

Ellen Hefferan
Co-Chair LSTA Accounting Committee